THE NATIONAL CITY BANK OF NEW YORK

1915

U. S. SECURITIES GOVERNMENT FINANCE AND FEDERAL RESERVE SYSTEM

NEW YORK, FEBRUARY, 1915.

Financial Conditions.

THE last month has witnessed a decided recovery of confidence in the position of the United States with regard to the present world crisis. When the upheaval came at the beginning of August the situation was so extraordinary and beyond all precedent that no reasonable forecast of the effects upon this country could be made. No one could doubt, however, that the effects would be very important, and everybody naturally proceeded immediately to safeguard himself against the worst that might come. This in itself created a very serious situation, and events have shown that apprehension went beyond the immediate dangers. The wild efforts made in the last days of July to sell European holdings of our securities directed attention to our most dangerous weakness in such a crisis, to-wit, the fact that very large amounts of European capital are employed in this country. That the state of affairs in Europe, and the appeal to the people of each country to sustain their government by subscribing to the war loans, would result in a return of our securities, was a perfectly reasonable expectation. How fast they would come no one could know, but it was apparent that they might come fast enough to keep the financial situation here in a state of demoralization for a long time. This danger, which happily has not materialized, but nevertheless was a very real danger, has been the chief cloud over the prospects of the United States since the war broke out. The events of the last two months have reduced this menace to an improbability.

The Federal Reserve Board, as a result of the inquiry instituted on the first of September reports that at that time the indebtedness of the United States to Europe, maturing within the next few months, was approximately $500,000,000. The merchandise balance of trade had been running against us since April, and our principal dependence for export, cotton, was without a market. Looking back at the situation even from safe ground there is no wonder that alarm was felt.

Since then the situation has radically changed. In the first place, the foreign holders of our securities have shown no eagerness to sell them. Various explanations are suggested for this, but it may be surmised that the most important are that as yet there has been no pressure upon them to do so and that they do not want to sell at prices that result in loss. The war loans have been offered upon terms that have enabled the public to take them without selling other holdings. Moreover, our listed securities that are held abroad are for the most part of high class, the returns upon them have been regular, many of them have been in the strong boxes of the owners for years, and there may well be an indisposition to dispose of them at a time when so much uncertainty overhangs Europe.

Present Balance of Trade.

In the second place, so great a change has occurred in our trade relations that we are now in position to take back our securities at a fairly rapid rate without embarrassment. In August the balance of trade was $19,400,396 against us, in September it was $15,048,722 in our favor, and since then the balances in our favor have been as follows: October, $57,305,074; November, $79,299,417; December, $131,863,077, with January unreported but probably as high as December. The indebtedness which in September looked so formidable has been paid off, and a credit balance has been accumulated which every week grows larger and becomes a bulwark of defense against any movement of securities this way which may develop in the future. It now appears to be demonstrated that the warring countries will all want to buy heavily of materials and supplies in this market during the continuance of the war. Several of the governments have made loans here, and others are negotiating, conditioned upon the use of the proceeds for purchases in this country. These loans are tangible offsets against any claim that may be created against this country. By reason of these accumulating credits the situation has become so secure that the gold pool to which over $100,000,000 was originally pledged, to provide a fund for the payment of adverse balances, has been dissolved and the assets distributed.

It is true that the large monthly trade balances in our favor have been due almost as much to a decline of imports as to an increase of exports, but until the war ends and industry in Europe has returned to a normal basis our importations are likely to be low. It is also to be considered that important amounts of railway notes maturing this year are held abroad and that these will have to be paid, but on the other hand the heavy expenditures abroad of American tourists will not be made this year.

The Security and Money Markets.

Under the influence of these favorable prospects the bond and stock markets have developed an excellent tone and prices have made a moderate advance. Capital has been accumulating and the owners have gained confidence to invest it. The first choice has been in short-term notes, as their early maturity will enable the purchaser to take advantage of any change in market conditions. The market now has been well cleared of municipal bonds, and high grade railway bonds have been bought freely. Easy money and low rates are encouraging the purchase of stocks, as many of them will carry themselves on borrowed money and yield a profit. The rising prices of bonds and stocks, however, have invited considerable sales from abroad, and this selling may be expected to follow every upward movement. The foreign government issues will be a constant factor in the world prices of securities until the full amount of them is out, and all have been actually absorbed and paid for.

Money has continued to work easier throughout the country. In the middle west the effect of good crops and high prices is appearing in rising bank deposits, the liquidation of indebtedness and a demand for commercial paper. The latter is in scarce supply. The Aldrich-Vreeland currency, of which $384,485,000 was issued, is being steadily reduced, and less than $100,000,000 remains outstanding, chiefly on account of banks in the South. The pool of $135,000,000 raised by subscription to lend money on cotton through the southern banks has had applications for only an insignificant amount, although the interest rate was reduced to five per cent. Evidently the Southern banks were able to satisfy their wants in a more convenient or satisfactory way. It is assumed that this pool, also, will be dissolved at an early day.

It occasions some surprise, however, to find that although the banks of New York City have been feeling very comfortable of late, and for the week ended January 22nd held reserves averaging $138,292,110 in excess of the present legal requirements, if calculation was made on the basis of the old law requiring reserves of 25 per cent. the same condition would have shown a deficit of $5,200,000.

Industrial Conditions.

The development of a sentiment of ease and security in the money markets is favorable of course to an industrial revival, but, although improvement may be noted, there has been no corresponding change in this respect. There has been a slight gain in iron and steel production, but the action of the steel corporation in discontinuing all dividends upon its common indicates that the outlook is still by no means clear. The prosperity of the grain and stock farmers is beginning to make itself felt in better trade in those sections. The best signs are where stagnation has been greatest, to wit, in the cotton goods industry and in the section producing cotton. The degree of improvement here, in view of all the conditions affecting cotton values, must be regarded as very satisfactory. The record since the cotton exchanges were reopened has demonstrated the usefulness of their facilities in stabilizing and sustaining the value of a large crop during the period while it is passing from the producers to the consumers. The service is easily understood. The farmer wants to sell his crop as soon as it is harvested; the spinners want to buy it as they need it throughout the year. If nobody buys cotton but the spinners, or in other words, if nobody buys simply for investment or speculation, the price is certain to sag off in the early part of the crop year, for spinners are not in position to buy the entire crop at once. The exchanges have developed a class of middlemen, call them investors, speculators or dealers, who are familiar with the trade and who buy and sell cotton. The exchanges enable them to buy without being obliged to actually receive, store and safeguard the staple itself. The market is thus broadened and the price fluctuations on the crop year are reduced to the minimum. Everybody has more confidence in a broad market which is the result of the consensus of opinion of everybody who is interested in cotton.

When the New York Exchange was reopened the first movement was the liquidation of certain old contracts by parties who desired to get out of the market even at a loss, but the market rallied, and since then the competition of investors, who have bought for the purpose of selling again, has unquestionably been a factor of strength. It has supported and strengthened the market and put confidence into the spinners themselves, so that the latter, feeling that the market was not dependent upon them alone, have dared to lay in supplies more freely than they had previously felt safe in doing. The New York market has led the southern markets in the advance.

With the price of cotton stabilized by a free broad market, the price of cotton goods was put on a firm basis, both at home and abroad, and merchants began to have confidence to buy more freely. The last half of January has seen an important change in this respect. The fear that the bottom would drop out of the market and that competitors would be able to buy goods at lower prices has largely passed away. Mill prices are stronger, although the prices of goods have not yet advanced as much as the prices of cotton; sales have been larger, manufacturers have gained confidence, the mills are running more steadily and unemployment is reduced.

With the exchanges open and cotton established on an eight-cent basis in the southern markets no artificial methods are required to finance the South. Capital flows freely to it, and with that section reimbued with confidence and reappearing as a purchaser in other markets a great factor in the country's internal trade is in good part restored. About one-third of the crop moved from first hands at a cent a pound or more below present prices.

After account is taken of these promising developments there is not much to say of actual changes. The railroads have been buying rails and some equipment to meet actual necessities, but they cannot enter upon any construction program with the security markets in their present state. They cannot go far on the strength of the recent rate deci-

sion, for while they were granted an advance of approximately five per cent., the decline in their revenues since the outbreak of the war has been much more than that. The latest month for which full returns are available is November, when the decline in gross was 13.4 per cent. from the same month in 1913. Moreover, the rate increase only applied to the lines east of Chicago, the application of the western lines being under hearing now. The roads have large amounts of short-term notes maturing this year which must be taken care of. These notes were issued because at the time the conditions were unfavorable to the sale of bonds, and the money so raised, for the most part, has been spent. The refunding provides no money for new work, and, so far as the notes are held in this country, does not involve a net demand on the investment market, but it is something to be gotten out of the way.

It is evident that there cannot be full employment for all of the country's industries unless at least an average amount of construction work is going on. The production of iron and steel, lumber, cement, copper, equipment of all kinds and many less important products is largely dependent upon new undertakings, and when these for the time being are laid aside or checked, a large amount of unemployment is unavoidable, and the reduced purchases of these industries and of their employes necessarily react upon the other industries.

A large part, much the larger part probably, of the savings of the country are invested locally and within the investor's own management or observation, and such investment will go on, affected only in minor degree by world conditions. Thus the record shows that in 154 cities of the central states the building permits issued in 1914 amounted to $771,017,852 as against $838,945,302 in 1913, a falling off of only eight per cent. In the localities where there have been good crops and good prices, or where the industries are prosperous, there will be expansion and construction, but the enterprises that must appeal to the general investment market will apparently have to face unfavorable conditions for some time to come.

The Use of Bank Credit for Constructive Work.

The action of the British government in serving notice that no foreign flotations will be permitted in the London market during the war without the approval of the government is notice that any new financing abroad will have to be done in the United States. It raises the interesting question of how much capital this country can supply. There is a large market for securities here, but it has never been large enough to absorb all of our own issues, and when it is considered that we must take many of these back from Europe, it is apparent that we will not begin to meet the demands at home and abroad unless there is a liberal use of bank credit.

Whether the member banks of the Federal Reserve system will be justified, in view of the present emergency, in allowing the margin of lending power released by the recent change in the law, to be taken up by loans based upon stock exchange collateral and other securities, is a question over which there will be a two-sided debate. The advocates of an aggressive national policy at this juncture in world affairs will favor it. They will point to the action of the great foreign banking organizations in waiving all rules that hamper them in dealing with the present situation, and say that this country at this time should display like courage in using its credit machinery. It will be said that we owe it as a duty to the world, while others are using their credit for destructive ends, to use our credit to sustain and build up industry. It will be said further that it would not be new in this country for bank loans to be made for fixed investments, that the legal reserves were lowered because compensating security had been provided in the Federal Reserve system, and that the situation would be as safe with the banks loaned up close to the new limit as under the old system with higher reserves. It will be argued that the chief danger from an expansion of unliquid credits lies in a movement of gold from the country, thus removing the base from a credit superstructure which cannot be correspondingly reduced, and that this danger can now be provided against by an international understanding that gold will not be shipped in any direction until after the war and normal conditions have been restored.

On the other hand it will be urged that the use of bank credit for long term or fixed investments is contrary to the spirit of the new banking law, that such loans cannot be rediscounted by the Federal Reserve banks, and that if they are taken freely by the member banks they will remain undigested until they can be absorbed by the real investment resources of the country; that whenever, in a fervor of investment enthusiasm, we have loaded the banks up with undigested securities, it has sooner or later been found necessary to slow up until they were worked off. The conservative financiers will point to the abnormal conditions existing, and insist that when so little can be known of the future it is not the part of wisdom or prudence to exhaust the bank reserves of the country in the making of unliquid loans.

It is safe to say that bankers are not going to buy securities on their own account. If there is an expansion of bank credit upon securities it must be because the public is buying and calling for accommodations. When it comes to that, each one of the 26,000 or more banks in the country will make its own policy toward its customers, but it may be added that under the competitive conditions that exist in the banking business in this country, the public, if aggressively in earnest about using its credit, has always been able to do so.

Six Months of War.

The war has now lasted six months, with expenditures upon a scale never before approached, and the ease with which they have been financed has occasioned general surprise. At the beginning, six months was frequently named as a period beyond which active hostilities could scarcely be carried for want of funds, but there is nothing in the present situation to indicate that they may not run on, so far as finances are concerned, for a long time. The official bank rate at London, Paris and

Berlin is five per cent., at Vienna five and one-half, and at Petrograd six per cent. It is true, however, that ordinary business demands are reduced and that the policies of these institutions are not governed at this time by the ordinary business considerations. Ease is artificially created by the liberality of their policies. The Bank of England, for example, early in the war took over some $350,000,000, or $400,000,000 of outstanding acceptances for the bill-brokers and banks of England, and gave cash credit for them on its books. Ordinarily these acceptances would have been liquidated in the course of the exchanges, but they were suddenly converted into credits available for any purpose. The supply of credit has been inflated to this extent and something similar has been done in other countries.

The London Economist has recently made the following calculation of the expenditures of the five principal combatants for the first six months:

Germany	$2,125,000,000	
Austria-Hungary	1,500,000,000	
		$3,625,000,000
Russia	2,125,000,000	
France	1,625,000,000	
United Kingdom	1,200,000,000	
		4,950,000,000
		$8,575,000,000

These figures are in excess of the loans that have been announced, but when the expenses of Japan, Turkey, Servia and Belgium, and of the neutral countries that have mobilized their troops, are included, it is probably safe to calculate that a year of war will require the raising of at least $15,000,000,000. Of course the financing of such expenditures can only be done by pyramiding credit. It is impossible for the government loans to be taken up out of current income; they can only be distributed by providing the public with means to buy the securities on credit, but when this is done there is no reason why the process may not continue so long as the public is willing to co-operate. The effect is to organize the private credit of the nation behind the public credit. The end would come when the people refused to pledge their private credit for the purchase of public securities or to give goods and services in exchange for credit. As yet there are no signs that the people are faltering in their support of any of the governments.

How War Expenditures are Paid.

A clearer view of the situation is had by dismissing the idea of raising money and thinking of the conduct of the war as a problem in the re-distribution of population. A portion of the population has been withdrawn from production for the army, and another portion is engaged in making war materials and supplies. It has been a subject of comment that there has been less distress among the people than was anticipated, but this is because they are being supported in large part by the expenditures from the war loans. War has become the principal business. But with this diversion of productive capacity, there must be a great curtailment in the ordinary industries, and this means that the people are not consuming as usual. Construction work is at a standstill and all classes are economizing. In this way a large part of the expenses of the war are met by going without the things that the people have been accustomed to have and by a halt in the normal progress. Where there has been no destruction of property the loss will be mainly in the failure to make normal progress, and in the loss of many of the most effective workers. It is evidently an error to include both expenditures and loss of production in the war costs, for the larger part of production is always absorbed by current consumption; or to count both expenditures and borrowings, for the latter are applied to the former. The payment of the indebtedness will involve only a transfer of capital, usually within the same country; the real loss occurred when the expenditures which the debts represent were made for an unproductive purpose. If, however, the taxation required to pay the interest and principal of the debts falls heavily upon necessaries it will impair the efficiency of the population and retard its progress. On the other hand, if the outcome of the war should be the establishment of peace on a basis which would permit of even partial disarmament and a reduction of military and naval establishments, the saving upon these expenditures might offset the interest upon a part or all of the new debts and even provide a sinking fund for their payment. If Europe has been spending, as currently reported, some $2,000,000,000 per year in preparations for war, and this could be reduced one-half, the saving would pay the interest on $25,000,000,000 at four per cent.

Wheat Exports and Prices.

Exports of wheat, flour included, from July 1, 1913, to January 1, 1915, were the heaviest on record for that period, aggregating 177,845,498 bushels. The value of the exports was $196,133,975, or an average of $1.10 per bushel. The highest exports in our history for wheat and flour occurred in the fiscal year 1902, when they amounted to 234,772,515 bushels, but the total value was only $178,537,196. The present fiscal year will surpass these figures both in bushels and value. Notwithstanding the enormous shipments from this country the stocks in Western Europe are only moderate and the governments are not trusting the purchase of supplies to the discretion of private dealers, but have sent official representatives to this country to buy on government account. They have bought persistently and taken the market away from the American millers, who are said to have been slow buyers. There is a congestion of grain at all the important seaports of this country, and all vessel room is engaged for several months to come. The latest information is that they are buying options on the 1915 crop. The advance in price from the low point on this crop has been about 65 cents per bushel, and the foreign consumer has not only to pay this, but an advance of several hundred per cent. in freight rates. One of the London dailies having suggested that the advancing prices called for a government inquiry, the *London Economist* comments upon the situation as follows:

Now if all that the Government wants is a simple and adequate explanation of this rapid rise, we can give it them

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at once, and save the expense and trouble and disastrous consequences of another Royal Commission. Not only are we at war, but Russia, our chief source of supply, is at war, and is unable, owing to the blockade of the Black Sea and the Baltic, to export her wheat crop—which, by the way, is not a good one. Then the Argentine harvest is reported to be suffering from bad weather. Two other big exporters are Australia and India. The wheat crop of the first has failed through drought, and the supplies of India are not over-abundant, if we may judge from the fact that the Indian Government has, rightly or wrongly, put a restriction on exports. Considering that in the Crimean War the price of wheat ran up to 74s, though our Government was at that time very tolerant of trading with the enemy, we ought not to be surprised at present prices, or that a further rise is prophesied.

The Department of Agriculture of the United States issued recently a bulletin showing the results of an investigation into the various charges levied upon wheat on its way from an American farmer to a foreign market. The investigation was made before the outbreak of the war, hence the figures are not applicable to present conditions, but they show what the charges were under normal conditions. The Department selects Kansas as a representative wheat state.

The outcome of the study is to show that, with wheat selling at (say) $1.17 per bushel in Liverpool, the division of the proceeds resulting from present methods gives the farmer about 87 cents. Of the 30 cents spent in marketing charges, one-tenth, or 3 cents, is taken by the country elevator, 15 cents goes for transportation to the sea-coast, 6 cents for ocean freight, a little over 1 cent for inspection at Galveston, and the remaining 5 cents for profit, insurance and minor items.

The middle man, or exporter, who is ordinarily supposed to make enormous profits on foodstuffs moving from producer to market, really gets only a very small return per unit handled. Some representative cases of actual shipments of wheat via New Orleans to Rotterdam show a margin of only 1 to 1¼ cents per bushel, or, with wheat at $1, 1 to 1¼ per cent. profit. This, moreover, is a gross earning, and out of it is deducted office expenses and cost of capital involved in the operation. The gains of the business come from the fact that the volume of grain handled is large, although this gain is offset by the fact that fluctuation of the risk element even in a slight measure, makes all the difference between profit and loss in the business. A fluctuation of as much as one-half of 1 cent either way wipes out the profit of many transactions, or doubles it, as the case may be. The exporter in making bids allows a gross margin as a rule of from 2½ to 3 cents, but out of this he must pay his charges for cables, interest, and a variety of others, averaging as a rule at least 1 cent per bushel. The Department of Agriculture investigators give details of eight specific transactions, each involving from 24,000 to 40,000 bushels, with the costs and expenses as well as the profits of each. The results show figures ranging from one-half cent of loss to 2¼ cents profit, but in three of the eight operations there was either a dead loss or practically no profit whatever; on three there were profits of 1¼ to 1.65 cents, and on only two did the profits exceed 2 cents per bushel, subject to the deductions already discussed above.

Canadian Borrowings.

Our Canadian neighbors will need to do some borrowing, and although it is not likely that the London market will be wholly closed to them it is probable that they will make an effort to satisfy their wants in the United States. Canada, it is well known, has been doing a vast amount of construction work in recent years. For a long time it had gained but slowly in population, the trend of migration from Europe being to the United States; but when the cheap lands of this country were practically exhausted there was a sudden awakening to the value of the prairie lands across our northwestern border, with the result that population poured into Canada, not only from the United Kingdom and Europe, but from the United States. To accommodate and encourage this movement, several trans-continental railways have been building and the development of cities and towns has gone on simultaneously, all requiring capital. These expenditures have been reflected in Canadian trade and our own exports to that country have grown by leaps and bounds.

Sir Edmund Walker, President of the Canadian Bank of Commerce, at the recent annual meeting of the stockholders of that institution, discussed the relations between the United States and Canada as follows:

> As soon as Great Britain begins to buy any new securities other than war issues, she will buy ours, and meantime we must hope that the market for our bonds in the United States will continue to grow. We cannot too often draw the attention of that country to the fact that when our foreign trade is analyzed the net debit for the difference between our sales and our purchases is payable to them and not to Europe. If the war prevents London from buying our securities, either the United States must buy them or our great trade with that country must fall away and the cry of "Made in Canada" would then have even a wider significance than it has today. During the year ending March, 1914, again omitting the figures for coin and bullion, we made purchases from the United States to the value of $409,818,000, and we sold them goods to the value of $178,282,000, so that with a net excess of imports from all countries of $179,945,000, the excess in the case of the United States was actually $231,536,000. Part of this is, of course, offset by the actual cash brought into Canada by settlers from the United States, part by investments made here by Americans, and part by the purchase of our securities, but it has mainly been settled in the past out of the proceeds of our sales of securities in London and on the Continent.

It is true that the trade relations between the two countries are very important to both, and it is certain that any aid that may be given to tide Canada over the present emergency and to sustain its purchasing power will be beneficial to our industries. The ability of Canada to increase its production of the food staples is an assurance that in the long run it will come out all right. The prospects now are that the area in wheat will be largely increased next year.

Domestic Acceptances.

There is evidently a developing interest in the proposal to amend the Federal Reserve Act to allow of bank acceptances in the domestic trade as already authorized in the foreign trade. A strong sentiment in favor of the policy existed when the

act was pending but in the last days of its consideration the privilege was limited to the foreign trade.

Mr. H. R. Eldridge, vice-president of this bank, in an address before the New York Credit Men's Association last month, laid emphasis upon the fact that in a country the size of the United States, trade between the States has substantially all the characteristics of the export and import trade. The bank acceptance has been established in the foreign trade until practically all purchases are made by its use, because it eliminates risks and serves the convenience of both buyer and seller. It relieves an unknown purchaser of the necessity of sending a remittance with his order, and the seller from the risk of shipping goods on the buyer's credit. These considerations are quite as important between dealers separated by long distances within the United States as between dealers separated by national boundaries.

Mr. Eldridge also brought out the importance of having a steady volume of domestic acceptances to supplement the supply of foreign acceptances in order to create a broad, trustworthy market for the latter. It is a perfectly familiar fact that you cannot have a reliable market for any commodity or kind of property unless a large number of buyers and sellers are participating in it and there is constantly a large volume of transactions. Otherwise the market is dependent upon a few, is untrustworthy and the public will not use it. Hence we cannot hope to make a reliable market for foreign bills in New York, or to popularize "dollar" exchange, unless we broaden the discount market by allowing our banks to create acceptances in the domestic trade. The volume of these, of course, would far exceed that of acceptances in the foreign trade. He said:

The market would be supplied with a plentiful number of bills of the highest order which would attract as purchasers not only the banks and investors of our own country, but, in times of peace, foreign banks and investors as well. The eligibility of such bills for rediscount with Federal Reserve banks (and undoubtedly for sale to those banks in open market transactions), would give them additional value. Indeed, they would form the most attractive class of investment we could have, as they would be immediately convertible into cash or bank credits whenever desired. They would form ideal secondary reserves for banks. Our discount markets would unquestionably absorb all the high grade bills offered at any time, and competition would permit them to sell at figures that would prove a revelation to the public.

It is quite clear that a discount market is one of the most important features of a financial system. Practically all the great nations, with the exception of our own, enjoy such markets.

Mr. Eldridge pointed out clearly how the interchange of investments would minimize the international movements of gold and steady all markets. He said:

The prime value of a discount market lies in the fact that when exchange rules against us and gold exports are threatened, investment in our bills by foreign bankers is peculiarly attractive, inasmuch as the rate must, of necessity, go high and foreign exchange coincidently invariably rules at rates promising a good profit in such transactions. It must be borne in mind that the protection of our gold reserve is vital to us all. Gold in the vault of a bank, or in the vaults of the Federal Reserve banks, is a basis for credit, and if credit is extended on the basis of, say, $4.00 for $1.00, it naturally follows that with every dollar of gold exported $4.00 of potential credit extension power goes with it, and if the surplus reserves of the country are not sufficient to conveniently permit such exports it means a contraction of at least $3.00 of credit for every gold dollar that leaves our shores.

With paper of this class on the market a sharp discrimination in rates would quickly be established in its favor and against single name paper, and particularly against the class of paper which signifies investment borrowing and that must be renewed again and again. A powerful influence would thus be brought to bear upon every business man to keep his affairs in the condition that would entitle him to use the bank acceptance.

Commenting upon the fact that a large amount of paper of a high class is now circulated through brokers Mr. Eldridge referred to the temptation offered to over-extension, and pointed out that if a home bank was accepting the paper a check would be established that would leave very little opportunity for over-extension.

The banker would, for a small consideration, become the sponsor of his credit. It goes without saying that paper of this nature is much to be preferred to the present style of commercial paper inasmuch as the Federal Reserve Act would not authorize the acceptance of such bills unless they were drawn to supply funds to be used in actual commercial transactions. The acceptance by the banks would be prima-facie evidence that the proceeds were to be so used. Such bills would unquestionably command in the open market a lower rate than that of what we now term commercial paper, and would afford the drawer an opportunity to avail himself of the cheapest money markets, thus tending to equalize credit all over the country.

Were domestic acceptances permitted it would be possible for a merchant in Kansas desiring to make his purchases in the cheapest market, even though there unknown, to do so if he were armed with a letter of credit from his banker to the effect that the bank would accept all bills drawn against it to the extent of an agreed figure, provided it is accompanied by a copy of the invoice and the original shipping documents. The only interest the seller would have would be to satisfy himself of the solvency of the accepting bank and the availability of the bill for sale in the open market.

The objection made to granting the acceptance privilege has been that the banks might in this manner increase their liabilities to a dangerous degree. It is apparently assumed that there is the same danger of an over-issue of acceptances as there might be of an over-issue of bank notes, but there is much difference between the two forms of credits. It is easier to over-issue paper in the form of small notes which can be paid out as money than paper issued in payment for merchandise and having a definite date of payment. The dealers in acceptances would be bankers, experienced, quick to detect any signs of irregularity, and all doubts would be publicly reflected in the market price of the paper. Upon this point he said:

The market would be sufficiently discriminating to separate the various classes of bills with keen regard to their financial strength, and that discrimination would be sufficient to eliminate rapidly from offerings all bills accepted by banks or houses of inadequate financial strength. No banker would permit his acceptances to be offered on an unresponsive market. The injury to his credit would be irreparable.

The compensation to the banks for acceptances would be small and banks in small towns probably would not find the privilege advantageous to them. They would profit more by having an abundance

of this class of paper available for investment and for a secondary reserve. Mr. Eldridge suggests that the law might require that banks authorized to give acceptances should carry slightly larger reserves; each bank could then make choice whether to use the privilege or not.

Appropriation Recommended to Make Effective Provision for Refunding Bonds into Treasury Notes.

The Secretary of the Treasury has submitted to Congress the following recommendation for legislation to cover the expenses of refunding the two per cent. government bonds into three per cent. one-year Treasury notes, according to the provision of Section 18 of the Federal Reserve Act:

TREASURY DEPARTMENT,
OFFICE OF THE SECRETARY,
Washington, December 18, 1914.

The SPEAKER, HOUSE OF REPRESENTATIVES.

SIR: In connection with section 18 of the Federal reserve act, which authorizes, under certain conditions, the refunding of 2 per cent. bonds of the United States into 1-year 3 per cent. Treasury notes or 30-year 3 per cent. United States bonds, which provision becomes effective on December 23, 1915, I have the honor to invite the attention of the Congress to the fact that no appropriation has been made for the expenses in the department incident to such refunding. The section in question provides that during a period of 20 years national banks desiring to reduce their circulation may offer to sell their bonds securing circulation, and that Federal reserve banks may be required quarterly to purchase the bonds offered, but not to exceed in total amount $25,000,000 annually. And, further, it is provided that Federal reserve banks may have issued to them by the Secretary of the Treasury in exchange for 2 per cent. bonds of the United States bearing the circulation privilege, but against which no circulation is outstanding, 30-year gold bonds and 1-year gold notes in the proportion of half and half, with the further provision that the Secretary of the Treasury may require the Federal reserve banks to purchase annually for 30 years an equal amount of similar notes to replace those maturing. Should the maximum operations authorized by the act take place each year it may result in the department being called upon each quarter to convert 2 per cent. bonds into 30-year bonds or into 1-year notes, the total amount of each for each year being $12,500,000, or an aggregate for each year of $25,000,000. In addition, after the first year, any notes maturing must be paid, and possibly new issues made to replace them. And the act further permits, at the request of any Federal reserve bank, the conversion of 1-year notes into 30-year bonds.

It is necessary for the department to prepare in advance for the conversions authorized, and these preparations will involve the preparation of plates, the purchase of paper, and the printing of the notes and bonds, together with the installation of certain equipment necessary to facilitate the work. For these preliminary expenses provision should now be made in order that the department may be in a position to make conversions authorized upon demand when this section of the law becomes effective. After the initial expenses it is believed the continuing expenses will be inconsiderable by comparison, and I think it will be possible to perform all the clerical work without additional employees.

The act of August 5, 1909, authorizing the issuance of 3 per cent. Panama Canal bonds, and the act of February 4, 1910, regarding certificates of indebtedness, each provides an indefinite appropriation of not to exceed one-tenth of 1 per cent. for the expenses of the issues. However, as it is impossible to estimate the amount of conversions that actually will be made during any particular period, and as certain of the expenses involved must be incurred without regard to the amount of bonds finally exchanged, it is suggested that authority be given for incurring expenses in proportion to the amount of conversions authorized. Accordingly, it is respectfully requested that an indefinite continuing appropriation be authorized at the present session of the Congress of an amount not to exceed one-tenth of 1 per cent. of the amount of conversions permitted the first year, and that thereafter a similar indefinite continuing appropriation be authorized of not to exceed one twenty-fifth of 1 per cent. of the amount permitted, such appropriations to continue while authority to convert exists.

It is my desire, in the interests of economy, that all expenses incurred by this department shall be kept at the minimum, and it will be my direction that all additional work thrown upon the department in connection with the conversions authorized shall, so far as possible, be absorbed in the general routine.

Respectfully,

W. G. MCADOO, *Secretary.*

Report of the Federal Reserve Board to Dec. 31, 1914.

The Federal Reserve Board has just issued its first report for the purpose of reviewing all phases

STATEMENT OF RESOURCES AND LIABILITIES OF EACH OF THE TWELVE FEDERAL RESERVE BANKS AT CLOSE OF BUSINESS JAN. 29, 1915.

(In Thousands of Dollars)

RESOURCES	Boston	N. Y.	Phila.	Clev'd	Rich'd	Atlanta	Chicago	St. Louis	M'npl's	Kas. City	Dallas	S. Fr'sco	Total
Gold coin and certificates	14,867	85,196	16,329	17,585	8,811	3,425	36,589	9,472	10,146	10,446	6,624	16,415	235,905
Legal tender notes, Silver certif's and Sub. coin...	2,588	7,090	4,918	998	82	2,472	531	888	10	590	634	81	20,882
Total................	17,455	92,286	21,247	18,583	8,893	5,897	37,120	10,360	10,156	11,036	7,258	16,496	256 787
Bills discounted and loans	177	1,014	317	425	3,720	3,180	1,623	476	216	143	1,449	1,215	13,955(c)
Investments...............	556	5,261	1,525	820			2,550		1,077	401		990	13,180
Due from other F.R. Banks net......................		19,833					1,955	1,794					7,421(b)
All other resources.......	1,069	2,555	1,318	201	34	181	1,649	2,541	229	71	748	295	10,891
TOTAL RESOURCES.....	19,257	120.949	24,407	20,029	12,647	9,258	44,897	15,171	11,678	11,651	9,455	18,996	302,234
LIABILITIES													
Reserve Deposits.........	17,091	117,345	19,367	16,877	7,645	5,917	42,344	14,133	8,902	9,670	6,756	13,469	279,516
Due to other F. R. Banks net (b)..................	435		2,721	597	3,006	1,683			1,800	873	1,142	3,904	
Federal Reserve notes in circulation—Net Amt....				119	840	794				74	451		2,278(a)
Capital Paid In............	1.731	3,604	2.319	2,436	1,156	864	2,553	1,038	976	1,034	1,106	1,623	20,440
TOTAL LIABILITIES....	19,257	120,949	24,407	20,029	12,647	9,258	44,897	15,171	11,678	11,651	9,455	18,996	302,234

(a) Total Reserve notes in circulation, 17,679. After deducting gold and lawful money in hands of Federal Reserve Agents, 15,401, for retirement of outstanding notes, the net liabilities of Reserve Banks upon outstanding notes, amount to 2,278.

(b) After deduction of items in transit between Federal Reserve Banks, 7,421, the Gold Reserve against Net Liabilities is 86%. and the cash reserve is 93.6%.

(c) Maturities of bills discounted and loans: 30 days, 6,331; 60 days, 4,903; Other maturities, 2,721; Total: 13,955.

of the work of the Board and apprising those who are interested of exactly what has been done.

The report, which is up to December 31, reviews the five months during which the system has been in operation; the Federal Reserve banks have been in actual operation for only two months of this time.

In part the report says:

"There is much yet to be done, but the work cannot be regarded as experimental in the sense that there is any uncertainty as to the outcome. The only question is as to how rapidly it will be possible to develop the full capabilities and resources of the Federal Reserve system."

The difficulties of establishing the system in the face of the economic disturbances occasioned by the European war, are pointed out, and the report also shows the value of the unusual relief measures approved by the Board which resulted in controlling and steadying financial conditions during this unsettled period.

In the course of a careful review of the history and outlook of the Federal Reserve system, the report covers early problems met by the Board. There are chapters on the effort of the Board to arrive at a method to regulate the purchase of paper, the discount policy, the gold fund, the cotton fund, the currency situation, open market operations, the clearing of checks, admission of State banks, functions of the Federal Advisory Council, and the general subject of administration.

A chapter in the report deals with the Place of Reserve Banks. From this chapter we quote the following:

"It should not, however, be assumed that because a bank is a Reserve Bank its resources should be kept idle for use only in times of difficulty, or, if used at all in ordinary times, used reluctantly and sparingly. Neither should it be assumed that because a Reserve Bank is a large and powerful bank all its resources should be in use all the time or that it should enter into keen competition with member banks, distributing accommodation with a free and lavish hand in undertaking to quicken unwisely the pace of industry. Such a policy would be sure, sooner or later, to invite disaster. Time and experience will show what the seasonal variations in the credit demands and facilities in each of the Reserve Banks of the several districts will be and when and to what extent a Reserve Bank may, without violating its special function as a guardian of banking reserves, engage in banking and credit operations. The Reserve Banks have expenses to meet, and while it would be a mistake to regard them merely as profit-making concerns and to apply to them the ordinary test of business success, there is no reason why they should not earn their expenses, and a fair profit besides, without failing to exercise their proper functions and exceeding the bounds of prudence in their management. Moreover, the Reserve Banks can never become the leading and important factor in the money market which they were designed to be unless a considerable portion of their resources is regularly and constantly employed. There will be times when the great weight of their influence and resources should be exerted to secure a freer extension of credit and an easing of rates in order that the borrowing community shall be able to obtain accommodation at the lowest rates warranted by existing conditions and be adequately protected against exorbitant rates of interest. There will just as certainly, however, be other times when prudence and a proper regard for the common good will require that an opposite course should be pursued and accommodations curtailed. Normally, therefore, a considerable proportion of its resources should always be kept invested by a Reserve Bank in order that the release or withdrawal from active employment of its banking funds may always exercise a beneficial influence. This is merely saying that to influence the market a Reserve Bank must always be in the market, and in this sense Reserve Banks will be active banking concerns when once they have found their true position under the new banking conditions. It would be a mistake, therefore, and a serious limitation of their usefulness to regard the Reserve Banks simply as emergency banks. Regulation in ordinary times, as well as protection in extraordinary times, may be expected to become the chief service which these institutions will perform. The Federal Reserve Board is fully alive to its opportunity and responsibilities in this respect, but it must counsel patience in awaiting the fruition of the new system. It will take time for the new banks to develop the technique of control and skill and experience in its application. The ascertainment of the correct base from which comprehensive operations should begin; the establishment of a normal level from which expansions and contractions will freely take place will have a most important bearing upon the future development and success of the system. Impatience to show results should not be permitted to tempt those in charge of the Reserve Banks into precipitate and unwise action.

"The vast and complex structure of modern banking and credit systems is one of extreme delicacy of balance and adjustments, and it must never be overlooked that it is highly sensitive to all manner of disturbances, as recent events have painfully demonstrated. The banking systems of the larger nations are closely related to one another, and financial distress or collapse at one point quickly transmits shock to all others. Safety for us in critical times will depend on the confidence our system commands, the strength of its reserves, and its power to bring them into action promptly and effectively if needed.

"In dealing with new districts and entirely changed banking methods, time and experience alone can supply the data necessary for charting the course to be pursued. This consideration, if nothing else, would suggest the greatest patience and prudence even if the European horizon were less clouded than it is to-day. None the less, the Board realized that where extraordinary conditions warrant extraordinary measures, it is the foremost duty of the Board and the banks to act promptly and boldly."

The report also contains an interesting and valuable group of exhibits, giving in detail the progress made in the organization of the system.

Federal Reserve Board Regulations and Circulars.

The following official documents of general interest have been issued by the Federal Reserve Board in Washington since the publication of our last bulletin:

Circular No. 1, announces a new series beginning with Jan. 1, 1915, and calls attention to probable modifications of previous orders.

Paper Offered for Rediscount.

Washington, January 12, 1915.

Circular No. 2.

ACCEPTANCE OF STATEMENTS IN LIEU OF CERTIFICATES AS TO CHARACTER OF COMMERCIAL PAPER.

The necessity of giving more time before regulation No. 3, of November 10, 1914, shall become effective is recognized by the Federal Reserve Board.

The accompanying regulation is therefore issued as below, and regulations Nos. 4 and 5, of 1914, a revision of which will shortly be published, will not go into effect until July 15, 1915.

CHARLES S. HAMLIN, *Governor.*

H. PARKER WILLIS, *Secretary.*

Regulation A.

(Superseding regulation No. 3 of Nov. 10, 1914.)

Whenever a member bank shall offer for rediscount any note, draft, or bill of exchange bearing the indorsement of such member bank, with waiver of demand notice and protest, the directors or executive committee of the Federal Reserve bank may, until July 15, 1915, accept as evidence that the proceeds of such note, draft, or bill of exchange were or are to be used for agricultural, industrial, or commercial purposes (and that such notes, drafts, or bills of exchange in other respects comply with the regu-

lations of the board) a written statement from the officer of the applying bank that of his own knowledge and belief the original loan was made for one of the purposes mentioned, and that the provisions of the act and regulations issued by the board have been complied with.

Regulation Regarding Commercial Paper.

WASHINGTON, *January 25, 1915*

COMMERCIAL PAPER.

Circular No. 3.

When Circular No. 13 bearing date of November 10, 1914, and the accompanying regulations were issued it was hoped that a period of two months would suffice to enable member banks to familiarize their customers with the requirements of Regulation No. 4 of 1914. It appears, however, that in many districts the needed readjustments of banking and business practice cannot be effected in so short a period. An extension of time was therefore asked by both member banks and their customers for the purpose of adjusting their methods to the new requirements and was granted by the Board (see Regulation A, accompanying Circular No. 2, Series of 1915).

In order to facilitate operations, particularly during the initial period, the requirements as to borrowers' statements have been modified. But while Circular No. 13, of November 10, 1914, is now superseded, the Board has not modified its views upon the general principles therein expressed as being of fundamental importance in the best development of the new system.

The Board has formulated in Regulation B, hereto annexed (paragraph III), a new method for certifying the eligibility of bills for rediscount. While banks will not be required to comply with the provisions of paragraph III until after July 15, the new method prescribed is made a part of this regulation in order that advance notice may be given to all banks, so that those which are equipped to do so may begin to operate under its provisions as soon as possible. The Board suggests, furthermore, that Federal Reserve Banks insist that the accompanying regulation be applied as promptly as possible to all so-called "purchased paper"—that is, paper bought through brokers or others with whom the purchasing bank has no direct business relations. Where such direct connections do not exist the requirement that statements, both as to business conditions and methods of borrowing, be furnished appears to be a matter of prudence and should not be postponed. In such cases as these, where borrowers' statements in the required form are not available until after the close of the business year, statements for the previous year may be accepted, pending receipt of new statement in required form, even though such statements may not contain all the desired data.

While it has been thought best not to insist upon a written statement in the case of limited borrowings by depositors, when officers of member banks, from their own personal knowledge, certify to the eligibility of the paper for discount, it is urged, nevertheless, that member banks do their utmost to accustom their borrowers to furnishing such statements.

WASHINGTON, *January 25, 1915*.

Regulation B.

COMMERCIAL PAPER.

The word "bill," when used in this regulation, shall be construed to include notes, drafts, or bills of exchange, and the word "goods" shall be construed to include goods, wares, merchandise, or staple agricultural products, including live stock.

I.

STATUTORY REQUIREMENTS.

The Federal reserve act provides that a bill, other than an acceptance (see Circular No. 5 and Regulation D, to be published shortly), to be eligible for rediscount by a member bank with a Federal Reserve Bank, must comply with the following statutory requirements:

(*a*) It must be indorsed by a member bank, accompanied by a waiver of demand, notice, and protest.

(*b*) It must have a maturity at the time of discount of not more than 90 days, except as provided by Regulation C, accompanying Circular No. 4, Series of 1915.

(*c*) It must have arisen out of actual commercial transactions; that is, be a bill which has been issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds of which have been or are to be used for such purposes.

(*d*) It must not have been issued for carrying or trading in stocks, bonds, or other investment securities except bonds and notes of the Government of the United States; but the pledge of goods as security for a bill is not prohibited.

II.

CHARACTER OF PAPER ELIGIBLE.

The Federal Reserve Board, exercising its statutory right to define the character of a bill eligible for rediscount at a Federal Reserve Bank, has determined:

(*a*) That it must be a bill the proceeds of which have been used or are to be used in producing, purchasing, carrying, or marketing goods in one or more of the steps of the process of production, manufacture, and distribution;

(*b*) That no bill is "eligible" the proceeds of which have been used or are to be used:

(1) For permanent or fixed investments of any kind, such as land, buildings, machinery (including therein additions, alterations, or other permanent improvements, except such as are properly to be regarded as costs of operation). It may be considered as sufficient evidence of compliance with this requirement if the borrower shows, by statement or otherwise, that he has a reasonable excess of quick assets over his current liabilities on open accounts, short-term notes, or otherwise;

(2) For investments of a merely speculative character, whether made in goods or otherwise.

III.

METHOD OF CERTIFYING ELIGIBILITY.

Any member bank applying for rediscount of a bill after July 15, 1915, must certify in its letter of application, over the signature of a duly authorized officer, that to the best of its knowledge and belief the bill was issued for one of the purposes mentioned in the above paragraphs and conforms to section 13 of the Federal Reserve Act and to this regulation.

It is recommended that every member bank maintain a file which shall contain original signed statements of the financial condition of borrowers, or true copies thereof, certified by a member bank or by a notary public, designating where the original statement is on file. Statements should contain all the information essential to a clear and correct knowledge of the borrower's credit and of his method of borrowing. A schedule specifying certain information, which it is desirable that such statements should include, is hereto appended.

Member banks shall certify in their letters of application for rediscount whether the paper offered for rediscount is depositor's or purchased paper, or paper rediscounted for other member banks, and whether statements are on file. When it does not appear that such statements are on file, except as hereinafter provided under (1), (2), and (3) below, the Federal Reserve Bank shall satisfy itself as to the eligibility of the paper offered for rediscount, and member banks will be expected to use such statement forms, identifying stamps, etc., as may be prescribed by the respective Federal Reserve Banks.

Any member bank rediscounting with a Federal Reserve Bank paper acquired from another member bank, with the indorsement of such member bank, may accept such member's certification regarding the character of the paper and the existence of the necessary statements.

Statements of the borrower's financial condition may be waived where bills offered for rediscount have been discounted by member banks for any of their depositors in the following cases:

(1) If the bill bears the signatures of the purchaser and the seller of the goods and presents prima facie evidence that it was issued for goods actually purchased or sold; or

(2) If the aggregate amount of obligations of such depositor actually rediscounted and offered for rediscount does not exceed $5,000, but in no event a sum in excess of 10 per centum of the paid-in capital of the member bank; or

(3) If the bill be specifically secured by approved warehouse receipts covering readily marketable staples:

Provided, however, That the bank shall certify to these conditions on the application blank in a manner to be designated by the respective Federal Reserve Banks.

CHARLES S. HAMLIN,
Governor.

H. PARKER WILLIS,
Secretary.

APPENDIX.

INFORMATION DESIRED IN CREDIT FILES OF MEMBER BANKS.

The credit files of member banks, referred to in the above regulation, should include information concerning the following matters:

(*a*) The nature of the business or occupation of the borrower;
(*b*) If an individual, information as to his indebtedness and his financial responsibility;
(*c*) If a firm or corporation, a balance sheet showing quick assets, slow assets, permanent or fixed assets, current liabilities and accounts, short-term loans, long-term loans, capital and surplus;
(*d*) All contingent liabilities, such as indorsements, guaranties, etc.;
(*e*) Particulars respecting any mortgage debt and whether there is any lien on current assets;
(*f*) Such other information as may be necessary to determine whether the borrower is entitled to credit in the form of short-term loans.

Six Months' Agricultural Paper.

WASHINGTON, *January 15, 1915.*

Circular No. 4.

The appended regulation is issued to supersede Regulation No. 5, of November 10, 1914, which is hereby revoked and canceled.

WASHINGTON, *January 15, 1915.*

SIX MONTHS' AGRICULTURAL PAPER.

Regulation C.

The word "bill" when used in this regulation shall be construed to include notes, drafts, or bills of exchange.

Each Federal Reserve Bank may receive for discount bills which have a maturity of more than three but less than six months, in an aggregate amount equal to a percentage of its capital stock to be fixed from time to time for each Federal Reserve Bank by the Federal Reserve Board.

Provided, however, That such bills are drawn or issued for agricultural purposes or are based on live stock; that is, that their proceeds have been used or are to be used for agricultural purposes, including the breeding, raising, fattening, or marketing of live stock; and

Provided further, That such bills comply in all other respects with each and every provision of Regulation B, series of 1915.

CHARLES S. HAMLIN,
Governor.

H. PARKER WILLIS,
Secretary.

Time Deposits and Savings Accounts.

Circular No. 6.

WASHINGTON, January 15, 1915.

The Federal Reserve Board deems it advisable to amplify its regulation relating to time deposits and savings accounts issued November 11, 1914, and to define under the following headings those deposits against which the Federal reserve act requires a reserve of only 5 per cent. to be maintained:

1. Time deposits, open accounts.
2. Savings accounts.
3. Certificates of deposit.

It was clearly not the intention of the act to permit a reduction of reserve to 5 per cent. upon deposits which may ordinarily be checked upon, but in respect to which a bank, by a blanket provision in its by-laws, may at any time require a withdrawal notice of not less than 30 days to be given. The reduction of the reserve to be carried against time deposits is intended to apply only to deposits under written agreement not to be withdrawn within 30 days from the date as of which the reserve calculation is made. Therefore, on the date of calculating reserve, under the definitions contained in the accompanying regulation, no deposit may be deemed a *time deposit,* whether on *open account* or on *certificate*—

(*a*) If it is payable within 30 days, because of the approaching end of the specified period for which it was deposited or because of receipt of notice of the date on which withdrawal will be made;

(*b*) If it may be withdrawn by check within 30 days, although the bank may have the right, by written contract or otherwise, to require a withdrawal notice of not less than 30 days.

Nor may any certificate of deposit be considered a time certificate if any part of the amount represented by it is subject to check or may be withdrawn without the presentation of the certificate for proper indorsement.

While savings accounts may at any time, by the action of the bank, be converted into time deposits, they are, nevertheless, ordinarily withdrawable on demand. In the absence of any statutory limitation upon the sum which may be received by a bank from any one individual as a savings account, the Board has no authority, for the purpose of calculating reserves, to impose any such limitation, but it feels strongly that in the interest of both the member banks and the Federal reserve system, the broad provisions of the act in respect to time deposits, savings accounts, and certificates of deposit, should not be made the means of any large general reduction of reserves by a transfer to those *forms* of deposits which are in *substance* demand deposits; and it is the purpose of the Board to countenance or permit a reduction of reserves to 5 per cent. *only* on deposits which are, in fact as well as in form, entitled to such reduction within the spirit of the act.

Banks carrying savings accounts must record them in separate ledgers which do not contain ordinary checking accounts or other items. Open time accounts and time certificates of deposit should also be carried in separate ledgers, but if carried in the same ledger with current checking accounts they must be grouped together so as to be readily distinguished from the latter.

The Board desires to make it clear that the act requires the full reserve, at the rate prescribed for demand deposits, to be carried against all savings accounts and all time deposits whether on open account or certificate, which are subject to check or which the bank has been notified are to be withdrawn within 30 days.

REGULATION GOVERNING TIME AND SAVINGS DEPOSITS.

Regulation E.

WASHINGTON, January 15, 1915.

Section 19 of the Federal reserve act provides, in part, as follows:

> "Demand deposits, within the meaning of this act, shall comprise all deposits payable within 30 days, and time deposits shall comprise all deposits payable after 30 days, and all savings accounts and certificates of deposit which are subject to not less than 30 days' notice before payment."

TIME DEPOSITS, OPEN ACCOUNTS.

The term "time deposits, open accounts" shall be held to include all accounts, not evidenced by certificates of deposit or savings pass books, in respect to which a written contract is entered into with the depositor at the time the deposit is made that neither the whole nor any part of such deposit may be withdrawn by check or otherwise except on a given date or on written notice given by the depositor a certain specified number of days in advance, in no case less than 30 days.

SAVINGS ACCOUNTS.

The term "savings accounts" shall be held to include those accounts of the bank in respect to which, by its printed regulations, *accepted by the depositor at the time the account is opened*—

(*a*) The pass book, certificate, or other similar form of receipt must be presented to the

bank whenever a deposit or withdrawal is made, and

(b) The depositor may at any time be required by the bank to give notice of an intended withdrawal not less than 30 days before a withdrawal is made.

TIME CERTIFICATES OF DEPOSIT.

A "time certificate of deposit" is defined as an instrument evidencing the deposit with a bank, either with or without interest, of a certain sum specified on the face of the certificate, payable in whole or in part to the depositor or on his order—

(a) On a certain date, specified on the certificate, not less than 30 days after the date of the deposit, or

(b) After the lapse of a certain specified time subsequent to the date of the certificate, in no case less than 30 days, or

(c) Upon written notice given a certain specified number of days, not less than 30 days before the date of repayment, and

(d) In all cases only upon presentation of the certificate at each withdrawal for proper indorsement or surrender.

CHARLES S. HAMLIN,
Governor.

H. PARKER WILLIS,
Secretary.

Purchase of Warrants.

WASHINGTON, *January 26, 1915.*

Circular No. 7.

In drawing Regulation F (attached), the Federal Reserve Board has been guided by the consideration that it is the primary purpose of the Federal Reserve Act to provide a banking organizaion which shall be responsive to the ebb and flow of commerce and trade.

Inasmuch as the funds of Federal Reserve Banks should be employed primarily in discount operations, purchases of warrants by such banks should be ordinarily limited to a relatively small proportion of their aggregate resources. This practice should be departed from only when general banking policy renders it advisable. In any and all cases the interest of the Federal Reserve Banks rather than that of the municipalities desiring to sell their obligations should be the primary consideration in making such investments.

In order to keep the assets of the Federal Reserve Banks in a liquid condition, investments in warrants, when made, should be made by preference in such as can be readily marketed, so that Federal Reserve Banks may be able to realize on them whenever it becomes desirable to enlarge their discounts of commercial paper.

In restricting Federal Reserve Banks to the purchase of such warrants as carry the definite assurance that the taxes and revenues will be actually in hand before maturity, the Board endeavors to follow the policy of the Act in restricting Federal Reserve Banks as far as possible to investments which are of short maturity and self-liquidating.

WASHINGTON, *January 26, 1915.*

STATUTORY REQUIREMENTS.

Regulation F.

Section 14 of the Federal Reserve Act reads in part as follows:

"Every Federal Reserve Bank shall have power—

(b) To buy and sell, at home or abroad, bonds and notes of the United States, and bills, notes, revenue bonds, and warrants with a maturity from date of purchase of not exceeding six months, issued in anticipation of the collection of taxes or in anticipation of the receipt of assured revenues by any State, county, district, political subdivision, or municipality in the continental United States, including irrigation, drainage, and reclamation districts, such purchases to be made in accordance with rules and regulations prescribed by the Federal Reserve Board."

For brevity's sake, the term "warrant" when used in this regulation shall be construed to mean "bills, notes, revenue bonds, and warrants with a maturity from date of purchase of not exceeding six months," and the term "municipality" shall be construed to mean "State, county, district, political subdivision, or municipality in the continental United States, including irrigation, drainage, and reclamation districts."

REGULATION.

The Federal Reserve Board has determined:

I. A Federal Reserve Bank may purchase such warrants as are issued by a municipality—

(a) In anticipation of the collection of taxes or in anticipation of the receipt of assured revenues. The taxes or assured revenues against which such warrants have been issued must be due and payable on or before the date of maturity of such warrants. For the purposes of this regulation taxes shall be considered as due and payable on the last day on which they may be paid without penalty;

(b) As the general obligations of the entire municipality; it being intended to exclude as ineligible for purchase all such obligations as are payable from "local benefit" and "special assessment" taxes when the municipality at large is not directly or ultimately liable;

(c) 1. Which has been in existence for a period of 10 years;

2. Which for a period of 10 years previous to the purchase has not defaulted, for longer than 15 days, in the payment of any part of either principal or interest of any funded debt authorized to be contracted by it; and

3. Whose net funded indebtedness does not exceed 10 per centum of the valuation of its taxable property, to be ascertained by the last preceding valuation of property for the assessment of taxes.

As a definition of the term "net funded indebtedness" as used in I (c) 3, above, and in further explanation of I (c) 1 and 2, relative to the term of existence of and non-default by the municipality, the Federal Reserve Board has adopted in substance the definitions and regulations of the board of trustees of the Postal Savings System, which, as printed hereunder as an appendix hereto, are made a part of these regulations.

II. Except with the approval of the Federal Reserve Board, no Federal Reserve Bank shall purchase and hold an amount in excess of 25 per centum of the total amount of warrants outstanding at any time and issued in conformity with provisions of section 14 (b) above quoted, and actually sold by a municipality.

III. Except with the approval of the Federal Reserve Board, the aggregate amount invested by any Federal Reserve Bank in warrants of all kinds shall not exceed at the time of purchase a sum equal to 10 per centum of the deposits kept by its member banks with such Federal Reserve Bank.

IV. Except with the approval of the Federal Reserve Board, the maximum amount which may be invested at the time of purchase by any Federal Reserve Bank in warrants of any single municipality shall be limited to the following percentages of the deposits kept in such Federal Reserve Bank by its member banks:

Five per centum of such deposits in warrants of a municipality of 50,000 population or over;

Three per centum of such deposits in warrants of a municipality of over 30,000 population but less than 50,000;

One per centum of such deposits in warrants of a municipality of over 10,000 population but less than 30,000.

V. Warrants of a municipality of 10,000 population or less shall be purchased only with the special approval of the Board.

The population of a municipality shall be determined by the last Federal or State census. Where it can not be exactly determined the Board will make special rulings.

VI. Opinion of recognized counsel on municipal issues or of the regularly appointed counsel of the municipalty as to the legality of the issue shall be secured and approved in each case by counsel for the Federal Reserve Bank.

VII. Any Federal Reserve Bank may purchase from any of its member banks warrants of any municipality, indorsed by such member bank, with waiver of demand, notice, and protest, up to an amount not to exceed 10 per centum of the aggregate capital and surplus of such member bank: *Provided, however,* That such warrants comply with provisions I and III of these regulations, except that where a period of 10 years is mentioned in I (*c*) hereof a period of five years shall be substituted for the purposes of this clause.

CHARLES S. HAMLIN,
Governor.

H. PARKER WILLIS,
Secretary.

DEFINITION OF "NET FUNDED INDEBTEDNESS."

The term "net funded indebtedness" is hereby defined to mean the legal gross indebtedness of the municipality (including the amount of any school district or other bonds which depend for their redemption upon taxes levied upon property within the municipality) less the aggregate of the following items:

(1) The amount of outstanding bonds or other debt obligations made payable from current revenues;

(2) The amount of outstanding bonds issued for the purpose of providing the inhabitants of a municipality with public utilities, such as waterworks, docks, electric plants, transportation facilities, etc.: *Provided,* That evidence is submitted showing that the income from such utilities is sufficient for maintenance, for payment of interest on such bonds, and for the accumulation of a sinking fund for their redemption;

(3) The amount of outstanding improvement bonds, issued under laws which provide for the levying of special assessments against abutting property in amounts sufficient to insure the payment of interest on the bonds and the redemption thereof: *Provided,* That such bonds are direct obligations of the municipality and included in the gross indebtedness of the municipality;

(4) The total of all sinking funds accumulated for the redemption of the gross indebtedness of the municipality, except sinking funds applicable to bonds just described in (1), (2), and (3) above.

DEFINITION OF "EXISTENCE" AND "NONDEFAULT."

Warrants will be construed to comply with that part of paragraph (*c*) of this regulation relative to term of existence and nondefault, under the following conditions:

(1) Warrants issued by or in behalf of any municipality which was, subsequent to the issuance of such warrants, consolidated with, or merged into, an existing political division which meets the requirements of these regulations, will be deemed to be the warrants of such political division: *Provided,* That such warrants were assumed by such political division under statutes and appropriate proceedings the effect of which is to make such warrants general obligations of such assuming political division, and payable, either directly or ultimately, without limitation to a special fund, from the proceeds of taxes levied upon all the taxable real and personal property within its territorial limits;

(2) Warrants issued by or in behalf of any municipality which was, subsequent to the issuance of such warrants, wholly succeeded by a newly organized political division, whose term of existence, added to that of such original political division or of any other political division so succeeded, is equal to a period of 10 years, will be deemed to be warrants of such succeeding political division: *Provided,* That during such period none of such political divisions shall have defaulted, for a period exceeding 15 days, in the payment of any part of either principal or interest of any funded debt authorized to be contracted by it: *And provided further,* That such warrants were assumed by such new political division under statutes and appropriate proceedings the effect of which is to make such warrants general obligations of such assuming political division, and payable, either directly or ultimately, without limitation to a special fund, from the proceeds of taxes levied upon all the taxable real and personal property within its territorial limits;

(3) Warrants issued by or in behalf of any municipality which, prior to such issuance, became the successor of one or more, or was formed by the consolidation or merger of two or more, preexisting political divisions, the term of existence of one or more of whch, added to that of such succeeding or consolidated political division, is equal to a period of 10 years, will be deemed to be warrants of a political division which has been in existence for a period of 10 years: *Provided* That during such period, none of such original, succeeding, or consolidated political divisions shall have defaulted, for a period exceeding 15 days, in the payment of any part of either principal or interest of any funded debt authorized to be contracted by it.

Waiver of Demand, Notice and Protest.

WASHINGTON, *January 27, 1915.*

Circular No. 8.

Section 13 of the Federal Reserve Act provides in part:

"Upon the indorsement of any of its member banks, with a waiver of demand, notice, and protest by such bank, any Federal Reserve Bank may discount notes, drafts and bills of exchange arising out of actual commercial transactions."

Attention is called to the fact that the waiver of demand, notice, and protest by the bank procuring the discount does not release the holder of the note or bill discounted from the duty to protest such note or bill in order that those indorsers who have not executed such a waiver may be held liable.

If the holder should fail to protest an indorsed note or bill at maturity, the Federal Reserve Bank might, in such circumstances, hold the member bank liable on account of the waiver executed, but other indorsers would be legally released.

Federal Reserve Banks are, therefore, cautioned to take all necessary steps to insure the protest of all maturing notes and bills which are in their possession or have been sent for collection through any correspondent bank wherever such notes or bills contain any indorsements not accompanied by a waiver of demand, notice, and protest. To insure this the bank or agent presenting any note or bill, held by the Federal Reserve Bank, at the place of payment at maturity should be instructed, if the same is dishonored, to immediately protest such note or bill and to have all necessary notices sent to the indorsers.

CHARLES S. HAMLIN,
Governor.

H. PARKER WILLIS,
Secretary.

Discount Rates at the Close of January.

The rates in force at the close of January at the different Federal Reserve Banks were as follows:

Class of Paper	Boston	New York	Philadelphia	Cleveland
30 days...	4½	4½	4	4½
60 days...	5	5	5	
90 days...	5	5	5	4½
Longer....	6	6	6	5½
	Richmond	**Atlanta**	**Chicago**	**St. Louis**
30 days...	4½	4	4	4½
60 days...		4	4	5
90 days...	5	4½	4½	5½
Longer....	5	4½	5	6
	Minneapolis	**Kansas City**	**Dallas**	**San Francisco**
30 days...	4½	4	4	4
60 days...	5		4½	4
90 days...	6	4½	4½	4½
Longer....	6	5½	5½	6